

GENERAL FUND ESTIMATED SURPLUS/(DEFICIT)

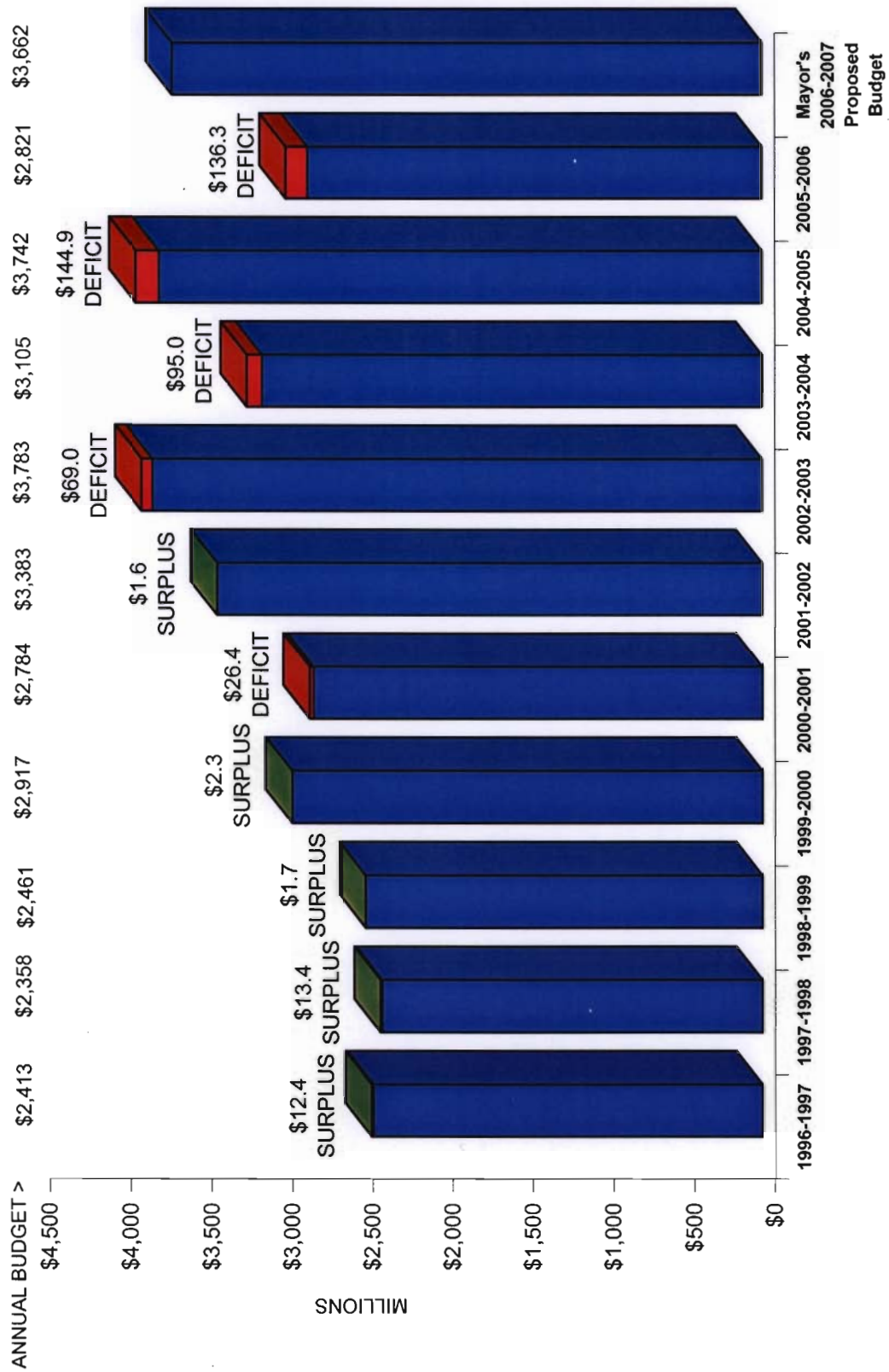
The Mayor's 2006-2007 Proposed Budget includes a General Fund deficit of \$62.8 million for fiscal year 2005-2006. The estimated deficit represents a \$132.3 million net shortfall in collections and net overspending in appropriations that is offset by \$69.5 million in one-time deficit reduction items. The deficit also assumes that appropriation surpluses from various departments totaling \$26.9 million will materialize.

The following table shows the components of both the Mayor's Proposed 2005-2006 General Fund deficit and the Office of Auditor General's (OAG) estimate. The proposed General Fund deficit assumes City Council's adoption of a budget amendment submitted by the Budget Department in September 2005, and the realization of certain revenue generating transactions totaling \$73.5 million. If these transactions are not realized at this amount, we estimate that the fiscal year 2005-2006 budget deficit could reach \$136.3 million.

| Surplus/(Deficit) by Agencies and Items/Deficit Reduction Components | Net Surplus/(Deficit) | Totals |
|---|-----------------------|------------------|
| Net Deficit from City Agencies | \$ (37,957,891) | \$ (37,957,891) |
| Deficit from Items: | | |
| Fringes | \$ (42,000,000) | |
| Prior Year Deficit | (43,202,874) | |
| Taxes and State Revenue Sharing | (9,178,266) | |
| Net Deficit from Operating Items | | (94,381,140) |
| Net Deficit from Agencies and Items | | \$ (132,339,031) |
| One Time Deficit Reduction Items: | | |
| POC Refinancing Amortization Savings | \$ 20,000,000 | |
| Greektown Garage Sale | 8,000,000 | |
| Risk Management Premium Under Funding | 30,000,000 | |
| Inventory and Equipment Sales | 10,000,000 | |
| Office Lease Rebates | 1,500,000 | |
| Total Deficit Reduction Components | | 69,500,000 |
| Mayor's Proposed 2005-2006 General Fund Deficit | | \$ (62,839,031) |
| Less Deficit Reduction Items Not Realized at April 24, 2006: | | |
| POC Refinancing | \$ (35,000,000) | |
| Inventory and Equipment Sales | (8,000,000) | |
| Office Lease Rebates | (1,500,000) | |
| Sales of Surplus Property | (29,000,000) | |
| Total Deficit Reduction Components Not Realized | | (73,500,000) |
| OAG's Deficit Estimate | | \$ (136,339,031) |

The OAG is not confident that the Administration will realize, by June 30, 2006, the entire \$73.5 million from refinancing Pension Obligations Certificates, selling of City's assets and properties, and lease rebates to offset the \$132.3 million deficit. Therefore, in the OAG's opinion, the Mayor's Proposed 2005-2006 General Fund deficit estimate of \$62.8 million is understated.

COMPARATIVE TOTAL FISCAL YEAR BUDGETS (INCLUDING ACTUAL SURPLUSES and DEFICITS) (In Millions)



RISK MANAGEMENT FUND

The Risk Management Fund is a self-insurance fund established by City Ordinance (Ord. No. 16-95) in 1995 to cover liability to third parties for any loss or damage arising out of negligence, tort, contract or otherwise accruing, payable by the City from and after July 1, 1994. The City may be liable under Workers' Compensation or Disability Benefits Law, or under any similar laws, or for damage to property or personal injury, in accordance with the applicable law.

The Risk Management Fund premium included in the Mayor's 2006-2007 Proposed Budget is compared to the fiscal year 2005-2006 Budget in the following schedule:

| | In Millions | | |
|---|--|---------------------|------------------------|
| | Mayor's 2006-2007 Proposed Budget | 2005-2006 Budget | Increase (Decrease) |
| Average Five Year Payout – General Fund and Transportation | \$ 62.0 | \$ 60.7 | \$ 1.3 |
| Anticipated Risk Management Cost Savings | 0.0 | (12.5) (A) | 12.5 |
| Net Premium before Earnings and Debt Service | \$ 62.0 | \$ 48.2 | \$ 13.8 |
| Earnings on Investments | (0.3) | (0.3) | 0.0 |
| Net Contribution to the Risk Management Fund from the General Fund and DDOT | \$ 61.7 | \$ 47.9 | \$ 13.8 |
| Debt Service | 21.4 | 21.4 | 0.0 |
| Annual Premium | <u>\$ 83.1</u> | <u>\$ 69.3 (B)</u> | <u>\$ 13.8</u> |

(A) A budget amendment, adopted before the beginning of the fiscal year 2005-2006, decreased the adopted Risk Management Fund premium by \$12.5 million to recognize cost savings anticipated in the fiscal year 2005-2006.

(B) The amount shown differs from the \$72.1 million included in the fiscal year 2005-2006 Budget. It appears that an additional \$2.8 million was budgeted in error.

Current Year Premium

Risk Management Fund revenues are premiums paid by the General Fund and Detroit Department of Transportation (DDOT), earnings from the investment of fund assets, and reimbursements from the State.

The calculation of the Risk Management Fund premium in the Mayor's 2006-2007 Proposed Budget is based on a five-year running average of actual payouts for damage claims, lawsuits, and other general and administrative expenditures from fiscal year 2000-2001 through fiscal year 2004-2005. The five-year historical average for the General Fund and the Department of Transportation is \$62.0 million as shown in the preceding chart. The budgeted premium for fiscal year 2006-2007 increased by \$13.8 million from the prior year. This is due in part to the inclusion, in the fiscal year 2005-2006 Budget, of a \$12.5 million deduction from the five-year average payout for the City's expected savings to be realized in the fiscal year 2005-2006 from contracting an outside agency to help the City reduce its exposure to future claims and judgments. Reducing the Risk Management Fund premium for future savings was a departure from the historical method of calculating the premium. Despite the departure, the City did not contract for that service in fiscal year 2005-2006.

Fund Balance

In 1995, pursuant to the Ordinance and Bond Resolution, the City issued \$100.0 million in self-insurance bonds. The proceeds were deposited in the Risk Management Fund to cover claim and lawsuit payments.

The following table shows the actual expenditures, revenues, excess or deficiency of revenues to cover current expenditures, and the fund balance of the Risk Management Fund for fiscal years 1994-1995 through 2004-2005 (the most recently completed fiscal year), an estimate for fiscal year 2005-2006 and the proposed budget for fiscal year 2006-2007.

| In Millions | | | | |
|-------------------|-----------------|-----------------|-------------------------------|--------------|
| Fiscal Year | Revenue | Expenditures | Excess/Deficiency of Revenues | Fund Balance |
| Beginning Balance | | | | \$ 100.0 |
| 1994-1995 | \$ 11.3 | \$ 48.8 | \$ (37.5) | 62.5 |
| 1995-1996 | 56.9 | 57.8 | (0.9) | 61.6 |
| 1996-1997 | 59.2 | 52.8 | 6.4 | 68.0 |
| 1997-1998 | 50.0 | 55.6 | (5.6) | 62.4 |
| 1998-1999 | 53.2 | 74.0 | (20.8) | 41.6 |
| 1999-2000 | 56.3 | 61.8 | (5.5) | 36.1 |
| 2000-2001 | 60.4 | 51.7 | 8.7 | 44.8 |
| 2001-2002 | 60.9 | 54.0 | 6.9 | 51.7 |
| 2002-2003 | 59.0 | 60.3 | (1.3) | 50.4 |
| 2003-2004 | 60.9 | 75.5 | (14.6) | 35.8 |
| 2004-2005 | 61.9 | 68.6 | (6.7) | 29.1 |
| 2005-2006 (A) | 18.5 | 44.6 | (26.1) | 3.0 |
| 2006-2007 (B) | 61.7 | N/A | N/A | |
| Total | <u>\$ 670.2</u> | <u>\$ 705.5</u> | <u>\$ (97.0)</u> | |

(A) For fiscal year 2005-2006, the contribution to the Risk Management Fund was budgeted at \$47.9 million. Of this amount, \$36.6 million was to be contributed from the General Fund and \$11.3 million from DDOT. The \$18.5 million estimate stated above includes DDOT's paid premium of \$11.3 million, a pending \$6.6 million contribution from the General Fund, as well as interest earnings. The claim expenditures have been annualized based on actual expenditures of the first nine months of fiscal year 2005-2006.

(B) The proposed budget amount is the only figure available for fiscal year 2006-2007.

As reflected in the preceding table, claim expenditures exceeded fund revenues by \$6.7 million in fiscal year 2004-2005 causing the balance of the Risk Management Fund to decrease to an all time low of \$29.1 million on June 30, 2005.

Section 18-8-18 of the City Code requires that the fund balance not fall below \$20.0 million. If the fund balance is expected to fall below \$20.0 million, the Finance Director must immediately advise the City Council of the deficiency and provide in the annual Risk Management Fund report to City Council a recommendation of the amount of any appropriation necessary to eliminate the deficiency by no later than the end of the fifth succeeding fiscal year following the fiscal year in which the deficiency arose. The Finance Director may recommend, subject to City Council approval, an increase or reduction in the minimum required balance. The Risk Management Fund balance was only \$9.1 million above the minimum required balance on June 30, 2005.

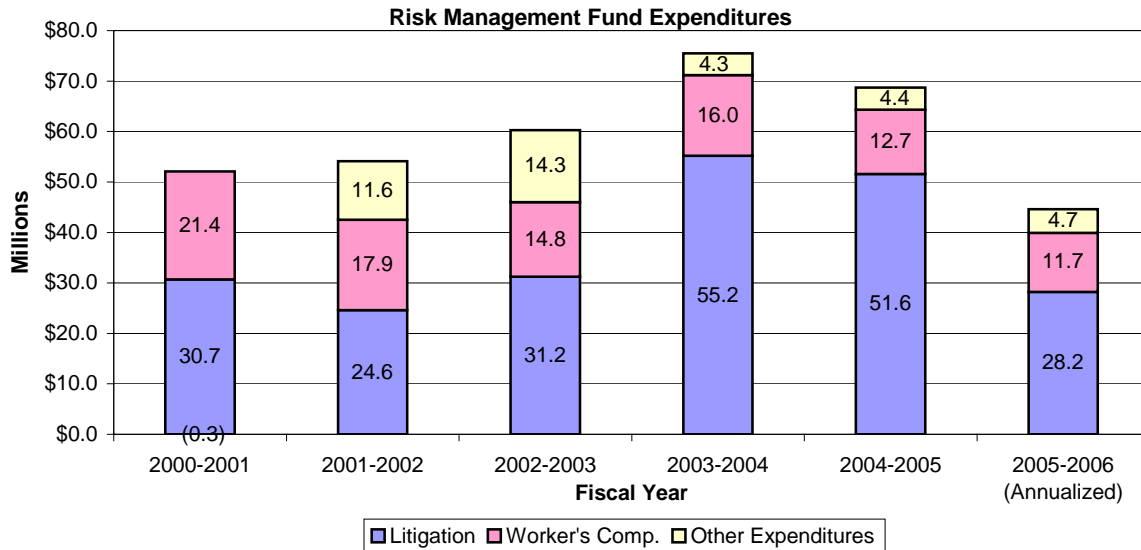
The budgeted premium for fiscal year 2005-2006 was \$47.9 million, which included a \$12.5 million reduction in the premium due to anticipated savings in claim expenditures. Risk Management Fund revenue was \$11.9 million and expenditures were \$33.5 million as of April 7, 2006. As a result, the fund balance as of April 7, 2006 was \$7.5 million, which is well below the minimum required balance of \$20.0 million. Due to anticipated additional savings in claims expenditures, the City has decided to fund only what is needed to cover claims. Therefore, only \$6.6 million of the budgeted \$36.6 million premium will be contributed from the General Fund for fiscal year 2005-2006.

The Budget Department has not provided its projection for fiscal year 2005-2006 Risk Management Fund expenditures, nor any support for the anticipated additional savings. The Budget Department has indicated that it will seek a recommendation from the Finance Director to reduce the required minimum Risk Management Fund balance.

Based on our analysis, the Risk Management Fund balance is projected to fall to \$3.0 million, and could fall to a deficit of \$3.6 million for fiscal year 2005-2006 if the \$6.6 million payment is not made. The fiscal year 2006-2007 budgeted Risk Management Fund premium does not include any funding to cover a deficit for fiscal year 2005-2006. We believe additional funding may be required.

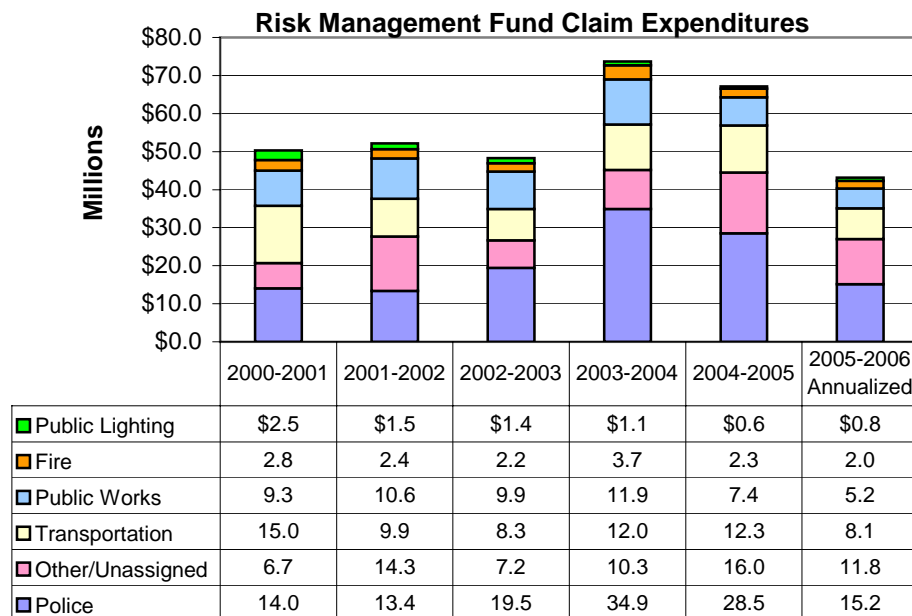
Expenditures

The Risk Management Fund premium is based on a five-year average of total expenditures, which includes damage claims, litigation, worker's compensation claims, and other general and administrative expenditures. The following chart shows the trend in total Risk Management Fund expenditures over the past five years.



As shown in the above chart, total expenditures were \$68.6 million in fiscal year 2004-2005. We have estimated expenditures to be \$44.6 million for fiscal year 2005-2006, an annualized amount based on expenditures recorded for the first nine months of the year. The decrease between the two years is \$24.0 million.

The following chart illustrates the trend in Risk Management Fund claim expenditures only, which excludes any general or administrative expenditures, and shows the expenditures by agency.



Debt Service

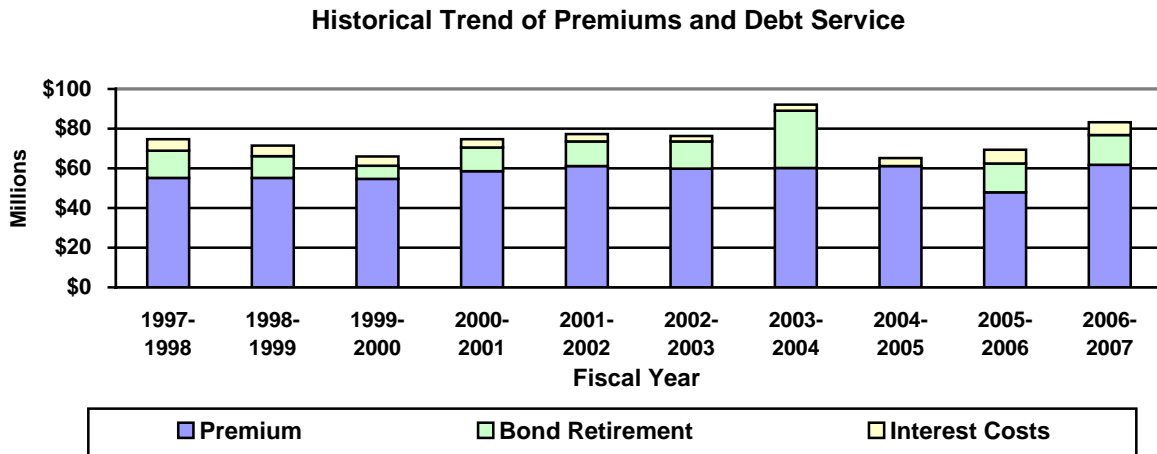
In fiscal year 2003-2004, the City issued an additional \$98.9 million in self-insurance bonds primarily to fund the fiscal year 2003-2004 Risk Management Fund premium, and to refinance the remaining balance of the original \$100.0 million self-insurance bond issue. Financing the claims premium, a current operating expenditure, with long-term debt was to be a one-time occurrence. However, in fiscal year 2004-2005 the City again issued \$62.3 million in self-insurance bonds to cover the annual premium amount for claims and litigation.

The table below shows the Budget Department's calculation of the annual premium for each of the ten fiscal years, from fiscal years 1997-1998 through 2006-2007, for claims and lawsuits against the City related to General Fund agencies and DDOT, and debt service (bond principal and interest) on the self-insurance bonds.

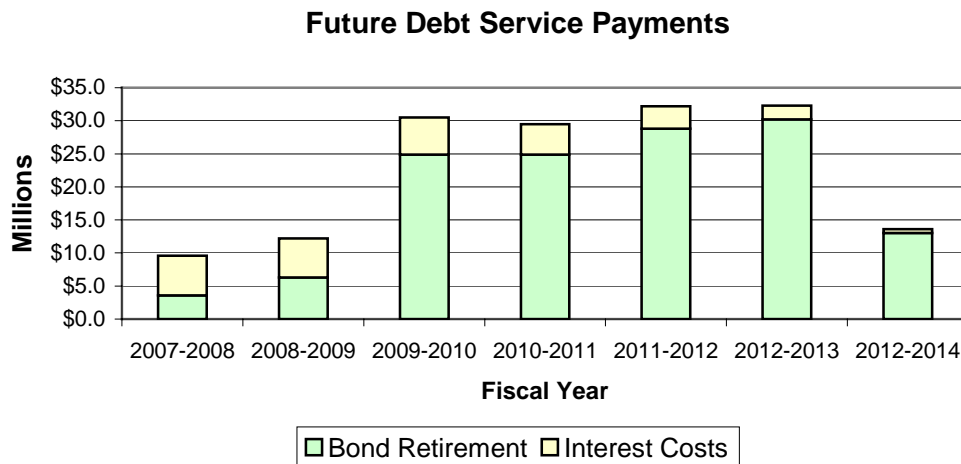
| Fiscal Year | General Fund | DDOT | Total Premiums | Net Bond Retirements | Bond & Interest Costs | Total Debt Service | Total Budgeted Appropriations |
|----------------|----------------|----------------|----------------|----------------------|-----------------------|--------------------|-------------------------------|
| 1997-1998 | \$ 45.2 | \$ 10.0 | \$ 55.2 | \$ 13.6 | \$ 5.9 | \$ 19.5 | \$ 74.7 |
| 1998-1999 | 45.7 | 9.5 | 55.2 | 11.0 | 5.2 | 16.2 | 71.4 |
| 1999-2000 | 45.4 | 9.3 | 54.7 | 6.6 | 4.6 | 11.2 | 65.9 |
| 2000-2001 | 46.6 | 12.0 | 58.6 | 11.9 | 4.2 | 16.1 | 74.7 |
| 2001-2002 | 48.6 | 12.5 | 61.1 | 12.5 | 3.6 | 16.1 | 77.2 |
| 2002-2003 | 47.9 | 12.0 | 59.9 | 13.6 | 2.8 | 16.4 | 76.3 |
| 2003-2004 | 46.3 | 13.9 | 60.2 | 28.9 | 3.0 | 31.9 | 92.1 |
| 2004-2005 | 47.3 | 13.8 | 61.1 | 0.0 | 4.0 | 4.0 | 65.1 |
| 2005-2006 | 36.6 | 11.3 | 47.9 | 14.6 | 6.8 | 21.4 | 69.3 |
| 2006-2007 | 49.8 | 11.9 | 61.7 | 14.9 | 6.5 | 21.4 | 83.1 |
| Ten Year Total | <u>\$459.4</u> | <u>\$116.2</u> | <u>\$575.6</u> | <u>\$127.6</u> | <u>\$46.6</u> | <u>\$174.2</u> | <u>\$749.8</u> |

As shown in the table above, the total Risk Management Fund appropriations for both premiums and debt service have ranged from a low of \$65.1 million in fiscal year 2004-2005 to a high of \$92.1 million in fiscal year 2003-2004. The fiscal year 2003-2004 appropriation included the retirement of the \$28.9 million remaining balance of the 1995 self-insurance bond issue, which was rolled into the 2003 bond issue. By the end of fiscal year 2006-2007, debt service will have added \$174.2 million to the risk management expense over ten years, an average of \$17.4 million per year. The average budgeted claims premium payment has been \$57.6 million during this ten-year period.

The following chart illustrates the trend in the risk management fund premium, bond retirement, and the interest cost the City has incurred, or expects to incur due to the debt service.



As of June 30, 2005, the current balances of the 2003 and the 2004 self-insurance bond issues are \$98.9 million and \$62.3 million respectively, for a total of \$161.2 million. Each of these bond issues mature over a ten-year period and should be paid off in fiscal years 2012-2013 and 2013-2014, respectively. The following chart illustrates the future debt service requirements for both bond issues.



Future Liabilities

The estimated total liability of the Risk Management Fund included in the June 30, 2005 Comprehensive Annual Financial Report was \$181.2 million. The current portion of this liability, payable within one year, was estimated at \$7.0 million, while the long-term portion of the liability was estimated at \$174.2 million. The total liability reflects a decrease of \$6.1 million from the prior year estimate of \$187.3 million. The average estimated total liability of the Risk Management Fund over the past 10 years was \$188.4 million.

Conclusion

Based on our analysis of the Risk Management Fund, we note these concerns:

- Only \$17.9 million of the \$47.9 million budgeted Risk Management Fund premium will be contributed in fiscal year 2005-2006 due to a change in the City's funding methodology. Based upon projected Risk Management Fund expenditures for fiscal year 2005-2006, the balance in the Risk Management Fund will fall below the \$20.0 million minimum level required by ordinance, and could fall to a deficit if the planned \$6.6 million General Fund payment is not made.
- The Budget Department anticipates a recommendation from the Finance Director to reduce the minimum legal balance in the Risk Management Fund. In order to obtain an approval, a plan to replenish the fund balance to the minimum requirement within five years must be presented. The Budget Department has not provided any analysis regarding planned savings or increases in future premiums needed to replenish the Fund Balance to the minimum legal balance. The Mayor's 2006-2007 Proposed Budget only includes funding for the annual premium and for debt service.
- The estimated annual average cost of debt service on the 2003 bond issue and the 2004 bond issue combined is \$21.1 million per year, over a period of ten years.
- The Risk Management Fund's bonded debt is more than five times higher than its fund balance as of June 30, 2005. The balance of the self-insurance bonds is \$161.2 million while the Risk Management Fund balance is only \$29.1 million as of June 30, 2005, the most recently completed fiscal year, and has been consistently decreasing. The Fund is highly leveraged, which will affect the Administration's ability to restore the Fund to the required minimum balance of \$20.0 million within five years.

DEPARTMENT OF TRANSPORTATION

The following schedule compares the Mayor's 2006-2007 Proposed Budget appropriations and revenues for the Detroit Department of Transportation (DDOT) operations, including the City's subsidy to the Detroit Transportation Corporation (DTC - "Detroit People Mover"), to the fiscal year 2005-2006 Budget:

| | In Millions | | |
|-----------------------------------|--|---------------------|------------------------|
| | Mayor's 2006-2007 Proposed Budget | 2005-2006 Budget | Increase (Decrease) |
| <u>Appropriations:</u> | | | |
| DDOT Operations | \$ 138.4 | \$ 138.5 | \$ (0.1) |
| DTC Support | 6.2 | 6.2 | - |
| Claims Fund | 16.2 | 15.5 | 0.7 |
| Capital Improvements – Bonds DTC | - | 10.0 | (10.0) |
| Total Appropriations | <u>\$ 160.8</u> | <u>\$ 170.2</u> | <u>\$ (9.4)</u> |
| <u>Revenues:</u> | | | |
| State Operating Assistance | \$ 51.4 | \$ 50.0 | \$ 1.4 |
| Farebox Revenue | 26.9 | 20.5 | 6.4 |
| General Fund Contribution to DDOT | 70.2 | 77.3 | (7.1) |
| General Fund Contribution to DTC | 6.2 | 6.2 | - |
| Other Operating Revenue | 1.3 | 0.8 | 0.5 |
| Claims Fund Revenue | 4.8 | 5.4 | (0.6) |
| Sale of G.O. Bonds | - | 10.0 | (10.0) |
| Total Revenues | <u>\$ 160.8</u> | <u>\$ 170.2</u> | <u>\$ (9.4)</u> |

The Mayor's 2006-2007 Proposed Budget is \$9.4 million less than the fiscal year 2005-2006 budget. Essentially, the two DDOT budgets are the same in total amount. Included in the fiscal year 2005-2006 budget are bond sales totaling \$10.0 million and the related appropriation for the vehicle mid-life overhaul of 12 Detroit People Mover (DPM) cars and the improvement of DPM stations and elevators. DDOT acts as a pass-through agency for the city subsidy to and capital funding of the DPM.

State Operating Assistance

Act 51, P.A. 1951 restricts State Operating Assistance for urban public transit agencies, with a population greater than 100,000, to an amount up to 50.0% of their eligible operating expenses, as defined by the State of Michigan Department of Transportation (MDOT). An eligible expense reimbursement formula is used to compute the amount of operating assistance that urban transit agencies receive from the State. An adjusted amount of eligible expenses is multiplied by a percentage, determined by the State, to calculate the amount of the distribution to transit agencies.

The Mayor's 2006-2007 Proposed Budget amount for State Operating Assistance is \$51.4 million, up \$1.4 million (3.0%) from the fiscal year 2005-2006 budget of \$50.0 million. The Budget Department used 32.4% of DDOT's fiscal year 2006-2007 budgeted eligible operating expenses to calculate the State Operating Assistance for fiscal year 2006-2007. The Office of the Auditor General (OAG) calculated \$54.4 million in State Operating Assistance for fiscal year 2006-2007, which is \$3.0 million (6.0%) more than the Budget Department's figure. The OAG used 33.1% in its calculation as advised by the MDOT Passenger Division on April 11, 2006. However, the actual amount DDOT will receive is based on the amount the State Legislature appropriates for Local Bus Operating Assistance, DDOT's actual eligible expenses, all eligible transit agencies' expenses, and the MDOT's disbursement formula. Based on our analysis, the Mayor's 2006-2007 Proposed Budget amount for State Operating Assistance is reasonable.

The following table shows budgeted and actual state operating assistance for fiscal years 2000-2001 through 2004-2005, budgeted and estimated state operating assistance for fiscal year 2005-2006, and the Mayor's 2006-2007 Proposed Budget amount for state operating assistance.

| Dollars In Millions | | | | | | |
|---------------------|------------------|----------------|----------------------------|------------|---|------------|
| Fiscal Year | Budgeted Revenue | Actual Revenue | Actual Over/(Under) Budget | | Increase/(Decrease) in Actual Revenue From Prior Year | |
| | | | Amount | Percentage | Amount | Percentage |
| 2000-2001 | \$ 58.7 | \$ 57.4 | \$ (1.3) | (2.2)% | N/A | N/A |
| 2001-2002 | 61.9 | 53.2 | (8.7) | (14.1) | \$ (4.2) | (7.3)% |
| 2002-2003 | 57.9 | 57.3 | (0.6) | (1.0) | 4.1 | (7.7) |
| 2003-2004 | 54.6 | 57.3 | 2.7 | 5.0 | 0.0 | 0.0 |
| 2004-2005 | 58.1 | 54.3 | (3.8) | (6.5) | (3.0) | (5.2) |
| 2005-2006 | 50.0 | (A) 52.6 | 2.6 | 5.2 | (1.7) | (3.1) |
| 2006-2007 | 51.4 | N/A | N/A | N/A | N/A | N/A |

(A) The amount shown in the table as actual revenue for fiscal year 2005-2006 is the estimated amount MDOT indicated DDOT will receive in state operating assistance.

N/A-Not Available

Farebox Revenue

Budgeted farebox revenue is \$26.9 million, up \$6.4 million (31.2%) from the fiscal year 2005-2006 Budget of \$20.5 million. The budget includes approximately \$3.0 million in farebox revenue from disabled riders. The proposed fare, subject to City Council approval, is seventy-five cents per disabled rider. The remaining increase in farebox revenue of \$3.4 million is based on DDOT's assumption that if gas prices continue to rise more people will ride the buses. DDOT projects 36,812,757 persons will ride buses in fiscal year 2006-2007 versus 35,396,882 in fiscal year 2004-2005. The projection for fiscal year 2005-2006 is 36,617,676 riders. Farebox revenue was \$21.8 million in fiscal year 2004-2005 without the disabled riders' fare and is estimated to be \$22.8 million for fiscal year 2005-2006 by the OAG. The OAG used actual farebox collections as of March 31, 2006 to annualize collections for the fiscal year. Since fiscal year 2000-2001, farebox collections have consistently been lower than budget. Based on this history and estimated farebox collections for fiscal year 2005-2006, and the uncertainty of obtaining the approval of City Council for the disabled rider fare, the budgeted amount for farebox revenue is overstated.

The following table shows budgeted and actual farebox revenue for fiscal years 2000-2001 through 2004-2005, budgeted and estimated farebox revenues for fiscal year 2005-2006, and the Mayor's 2006-2007 Proposed Budget amount for farebox revenue.

| Dollars In Millions | | | | | | |
|---------------------|------------------|----------------|----------------------------|------------|---|------------|
| Fiscal Year | Budgeted Revenue | Actual Revenue | Actual Over/(Under) Budget | | Increase/(Decrease) in Actual Revenue From Prior Year | |
| | | | Amount | Percentage | Amount | Percentage |
| 2000-2001 | \$ 32.0 | \$ 24.4 | \$ (7.6) | (23.8)% | N/A | N/A |
| 2001-2002 | 27.0 | 23.4 | (3.6) | (13.3) | \$ (1.0) | (4.1)% |
| 2002-2003 | 31.3 | 24.4 | (6.9) | (22.0) | 1.0 | 4.3 |
| 2003-2004 | 31.3 | 24.1 | (7.2) | (23.0) | (0.3) | (1.2) |
| 2004-2005 | 29.1 | 21.8 | (7.3) | (25.1) | (2.3) | (9.6) |
| 2005-2006 | 20.5 | (A) 22.9 | 2.4 | 11.7 | 1.1 | 5.0 |
| 2006-2007 | 26.9 | N/A | N/A | N/A | N/A | N/A |

(A) The amount shown in the table as actual revenue for fiscal year 2005-2006 is an Office of the Auditor General estimate, based on actual year-to-date farebox revenue as of March 31, 2006 annualized through the end of the fiscal year 2005-2006.

N/A-Not Available

General Fund Contribution - DDOT

The budgeted General Fund Contribution (Subsidy) to DDOT is \$70.2 million for fiscal year 2006-2007, a decrease of \$7.1 million (9.18%) from the fiscal year 2005-2006 budget of \$77.3 million. In fiscal year 2006-2007, DDOT plans to fund \$7,993,771 of its operating costs with Federal Transit Administration (FTA) grants rather than with general fund money as follows:

- \$981,500 for contractual service costs for the full implementation of the Lawson software (a financial application software) and new fareboxes,
- \$100,000 for rentals, contracts and equipment,
- \$311,409 for three administrative positions, and
- \$6,600,862 for salaries and fringes of 83 automotive mechanics.

Based on historical subsidies to DDOT and the five-year average subsidy of \$76.1 million, the \$70.2 million subsidy is not reasonable, as the table on the following page shows. However, FTA grants can be used for operating costs, such as inventories, salaries and wages, and contracts. The estimated subsidy for fiscal year 2005-2006 is \$71.2 million. Therefore, because the DDOT is using FTA grants in fiscal year 2006-2007 to cover a portion of its operating expenses, the budgeted subsidy is reasonable.

The following table shows budgeted and actual general fund contributions to DDOT for fiscal years 2000-2001 through 2004-2005, the budgeted and estimated general fund contribution to DDOT for fiscal year 2005-2006, and the Mayor's 2006-2007 Proposed Budget amount for the general fund contribution to DDOT.

| Fiscal Year | Dollars In Millions | | | | | |
|----------------|---------------------|-------------------|-------------------------------|------------|---|------------|
| | Budgeted Revenue | Actual Revenue | Actual Over/(Under) Budget | | Increase/(Decrease) in Actual Revenue From Prior Year | |
| | | | Amount | Percentage | Amount | Percentage |
| 2000-2001 | \$ 63.2 | \$ 74.2 | \$ 11.0 | 17.4% | \$ 14.0 | 23.3% |
| 2001-2002 | 73.4 | 79.4 | 6.0 | 8.2 | 5.2 | 7.0 |
| 2002-2003 | 67.6 | 75.5 | 7.9 | 11.7 | (3.9) | (4.9) |
| 2003-2004 | 57.6 | 74.3 | 16.7 | 29.0 | (1.2) | (1.6) |
| 2004-2005 | 69.6 | 77.4 | 7.8 | 11.2 | 3.1 | 4.2 |
| 2005-2006 | 77.3 | (A) 71.2 | (6.1) | (7.9) | (6.2) | (8.0) |
| 2006-2007 | 70.2 | N/A | N/A | N/A | N/A | N/A |

(A) The amount shown in the table as actual revenue for fiscal year 2005-2006 is an Office of the Auditor General estimate, based on actual year-to-date general fund contributions to DDOT as of March 31, 2006 annualized through the end of the fiscal year 2005-2006.

N/A-Not Available

DDOT Operations

The Mayor's 2006-2007 Proposed Budget includes \$2.6 million in employee turnover savings. The Budget Department expects turnover savings from the elimination of seven vacant positions, retirements, resignations, terminations, employees on leaves of absence, and employees receiving workers' compensation.

The Mayor's 2006-2007 Proposed Budget includes \$9.4 million in overtime. As of March 31, 2006, DDOT's overtime was \$10.7 million. The budgeted amount for overtime for fiscal year 2005-2006 is \$9.5 million. Based on actual overtime to date, overtime is underestimated for fiscal year 2006-2007. A representative from DDOT indicated that it is mandated to limit overtime to the budget. The Budget Department communicated that the Mayor's Office and the Budget Department will monitor DDOT's overtime. The Mayor's 2006-2007 Proposed Budget amount for DDOT overtime is optimistic.

In our prior audit report, we noted that the MDOT was withholding approximately \$1.0 million per month in state operating assistance because DDOT was not in compliance with its operable wheelchair lift requirement. In June 2005, MDOT determined that DDOT complied with the wheelchair lift requirement and released all withheld funds to DDOT.

Net Operating Losses

The pattern of the DDOT's net operating losses is well documented, as are the public policy reasons underlying continued subsidies to transit operations. The following schedule details the DDOT's actual and expected net operating losses over recent years. The data for this schedule was obtained from the City's Comprehensive Annual Financial Report (CAFR) for fiscal years ended June 30, 2000 through June 30, 2005, Budget Department data for fiscal year ending June 30, 2006, and the Mayor's 2006-2007 Proposed Budget.

| Fiscal Year | In Millions | | | |
|---------------|--------------------------|--------------------------|--------------------|---------------------------------|
| | Operating Revenue (A) | Operating Expense (B) | Net Operating Loss | Transfers from the General Fund |
| 1999-2000 | \$ 29.0 | \$ 172.6 | \$ 143.6 | \$ 60.2 |
| 2000-2001 | 25.1 | 187.1 | 162.0 | 74.2 |
| 2001-2002 | 24.1 | 187.4 | 163.3 | 79.4 |
| 2002-2003 | 25.2 | 196.2 | 171.0 | 75.5 |
| 2003-2004 | 24.7 | 206.6 | 181.9 | 74.3 |
| 2004-2005 | 23.0 | 196.2 | 173.2 | 77.4 |
| 2005-2006 | (C) 24.1 | (D) 153.9 | 129.8 | 77.3 |
| 2006-2007 (E) | 28.2 | 154.5 | 126.3 | 70.2 |

(A) Operating revenue consists primarily of farebox revenue.

(B) Operating expenses do not include the DTC subsidy.

(C) Operating revenue for fiscal year 2005-2006 is an estimate.

(D) Operating expense for fiscal year 2005-2006 is the budget amount.

(E) Operating revenue, operating expense, net operating loss, and transfers from the general fund are the Mayor's 2006-2007 Proposed Budget amounts.

N/A-Not Available

The preceding table shows that operating expense declined by \$42.3 million when comparing the \$196.2 million actual amount for fiscal year 2004-2005 to the budgeted amount for fiscal year 2005-2006. The \$153.9 million budgeted operating expense was understated, because it was based on assumptions that were not realized, like the transfer of DDOT to DARTA. The fiscal year 2005-2006 and 2006-2007 budgets for operating expense do not include expenses that will be funded with federal grant revenues. The DDOT does not include revenue from federal grants in its budgets, nor does DDOT include amounts in its appropriations that will be funded with federal grant revenue.

Financial Trend Analysis

The OAG analyzed DDOT farebox revenue, revenue from use of assets, miscellaneous receipts and other financing sources, salaries and wages, and operating expenses for fiscal years 2003-2004, 2004-2005, and 2005-2006. Amounts for fiscal year 2005-2006 were annualized. The revenue and expense data were analyzed to determine if trends indicate that DDOT is increasing its revenue and reducing its costs. The trend for farebox revenue indicates the revenue is relatively stable. Revenue from use of assets is rising. However, the trend for miscellaneous receipts and other financing sources is moving downward. Salaries and wages are relatively stable. However, operating expenses are on a downward trend. In summary, the trends indicate operating revenues are relatively stable and operating expenses are declining.

DDOT indicated that it has begun upgrading its Gilbert facility and will continue upgrading it in fiscal year 2006-2007. The upgrades will provide DDOT with modernized equipment, thereby making DDOT more efficient and cost-effective. DDOT has reduced its costs by upgrading the facility. DDOT's Lawson System was also upgraded by adding an accounts payable module, a general ledger module, and a purchasing module. These modules have made DDOT more efficient and cost-effective.

DDOT plans to upgrade its Shoemaker and Coolidge facilities in fiscal year 2006-2007, eliminate its boilers, and upgrade its Lawson System to eliminate waste and obsolete inventories. The Lawson System will also be upgraded to keep track of vehicle maintenance work orders, warranties, and parts, and to hold mechanics accountable. These initiatives will reduce DDOT's costs and make DDOT more efficient. To increase revenue, DDOT plans to charge disabled riders a seventy-five cent fare.

Conclusion

Based on our analysis, the budgeted revenues and appropriations included in the Mayor's 2006-2007 Proposed Budget for DDOT are reasonable; however, we believe that farebox revenue is overstated and overtime is understated. If the increase in farebox revenue is not realized, or overtime exceeds the amount in the Mayor's 2006-2007 Proposed Budget, or a combination of both, an increase in the General Fund subsidy may be required.